

**REPORT OF THE AUDIT OF THE
FORMER HARLAN COUNTY
SHERIFF'S SETTLEMENT - 2005 TAXES**

May 31, 2006



**CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS
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EXECUTIVE SUMMARY
AUDIT EXAMINATION OF THE
HARLAN COUNTY
SHERIFF'S SETTLEMENT - 2005 TAXES

May 31, 2006

The Auditor of Public Accounts has completed the audit of the Sheriff's Settlement - 2005 Taxes for the former Harlan County Sheriff as of May 31, 2006. We have issued an unqualified opinion on the financial statement taken as a whole. Based upon the audit work performed, the financial statement is presented fairly in all material respects.

Financial Condition:

The former Sheriff collected taxes of \$6,703,182 for the districts for 2005 taxes, retaining commissions of \$280,037 to operate the Sheriff's office. The former Sheriff distributed taxes of \$6,422,940 to the districts for 2005 Taxes. Taxes of \$142 are due to the districts from the former Sheriff and refunds of \$224 are due to the former Sheriff from the taxing districts.

Report Comment:

The Former Sheriff's Office Lacked Adequate Segregation Of Duties

Deposits:

The former Sheriff's deposits were insured and collateralized by bank securities.

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CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky

Honorable Steven L. Beshear, Governor

Jonathan Miller, Secretary

Finance and Administration Cabinet

Honorable Joseph A. Grieshop, Harlan County Judge/Executive

Honorable Steve Duff, Former Harlan County Sheriff

Honorable Marvin Lipford, Harlan County Sheriff

Members of the Harlan County Fiscal Court

Independent Auditor's Report

We have audited the former Harlan County Sheriff's Settlement - 2005 Taxes as of May 31, 2006. This tax settlement is the responsibility of the former Harlan County Sheriff. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, and the Audit Guide for Sheriff's Tax Settlements issued by the Auditor of Public Accounts, Commonwealth of Kentucky. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, the Sheriff's office prepares the financial statement on a prescribed basis of accounting that demonstrates compliance with the modified cash basis, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the accompanying financial statement referred to above presents fairly, in all material respects, the former Harlan County Sheriff's taxes charged, credited, and paid as of May 31, 2006, in conformity with the modified cash basis of accounting.

In accordance with Government Auditing Standards, we have also issued our report dated July 24, 2007 on our consideration of the former Sheriff's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to



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provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Based on the results of our audit, we present the accompanying comment and recommendation, included herein, which discusses the following report comment:

- The Former Sheriff's Office Lacked Adequate Segregation Of Duties

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Crit Luallen", with a long horizontal flourish extending to the right.

Crit Luallen

Auditor of Public Accounts

July 24, 2007

HARLAN COUNTY
STEVE DUFF, FORMER SHERIFF
SHERIFF'S SETTLEMENT - 2005 TAXES

May 31, 2006

<u>Charges</u>	County Taxes	Special Taxing Districts	School Taxes	State Taxes
Real Estate	\$ 1,351,281	\$ 736,835	\$ 1,502,578	\$ 652,199
Tangible Personal Property	571,541	280,681	563,693	645,744
Intangible Personal Property				97,571
Franchise Taxes	231,807	115,721	225,825	
Additional Billings	3,647	1,997	4,792	1,769
Oil and Gas Property Taxes	38,262	20,973	52,008	18,564
Limestone, Sand and Mineral Reserves	683	374	928	331
Bank Franchises	71,743			
Penalties	16,830	9,185	18,599	8,353
Adjusted to Sheriff's Receipt	3	31	6	17
Gross Chargeable to Sheriff	<u>2,285,797</u>	<u>1,165,797</u>	<u>2,368,429</u>	<u>1,424,548</u>
<u>Credits</u>				
Exonerations	5,207	2,852	6,864	2,669
Discounts	28,481	14,215	28,561	20,935
Delinquents:				
Real Estate	86,550	47,378	104,213	41,936
Tangible Personal Property	10,816	5,321	10,316	12,660
Intangible Personal Property				628
Franchise Taxes (Uncollected)	<u>41,300</u>	<u>21,706</u>	<u>48,781</u>	
Total Credits	<u>172,354</u>	<u>91,472</u>	<u>198,735</u>	<u>78,828</u>
Taxes Collected	2,113,443	1,074,325	2,169,694	1,345,720
Less: Commissions *	<u>90,109</u>	<u>45,659</u>	<u>86,788</u>	<u>57,481</u>
Taxes Due	2,023,334	1,028,666	2,082,906	1,288,239
Taxes Paid	2,023,172	1,028,581	2,083,003	1,288,184
Refunds (Current and Prior Year)	<u>68</u>	<u>37</u>	<u>92</u>	<u>90</u>
Due Districts or (Refunds Due Sheriff) as of Completion of Audit	<u>\$ 94</u>	<u>\$ 48</u>	<u>\$ (189)</u>	<u>\$ (35)</u>

* and ** See Next Page.

The accompanying notes are an integral part of this financial statement.

HARLAN COUNTY
STEVE DUFF, FORMER SHERIFF
SHERIFF'S SETTLEMENT - 2005 TAXES
May 31, 2006
(Continued)

* Commissions:

10% on	\$	10,000
4.25% on	\$	4,523,488
4% on	\$	2,169,694

** Special Taxing Districts:

Library District	\$	16
Health District		11
Extension District		19
Soil Conservation District		<u>2</u>
Due Districts	\$	<u><u>48</u></u>

HARLAN COUNTY
NOTES TO FINANCIAL STATEMENT

May 31, 2006

Note 1. Summary of Significant Accounting Policies

A. Fund Accounting

The Sheriff's office tax collection duties are limited to acting as an agent for assessed property owners and taxing districts. A fund is used to account for the collection and distribution of taxes. A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

B. Basis of Accounting

The financial statement has been prepared on a modified cash basis of accounting. Basis of accounting refers to when charges, credits, and taxes paid are reported in the settlement statement. It relates to the timing of measurements regardless of the measurement focus.

Charges are sources of revenue which are recognized in the tax period in which they become available and measurable. Credits are reductions of revenue which are recognized when there is proper authorization. Taxes paid are uses of revenue which are recognized when distributions are made to the taxing districts and others.

C. Cash and Investments

At the direction of the fiscal court, KRS 66.480 authorizes the Sheriff's office to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

Note 2. Deposits

The former Sheriff maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC) as required by KRS 66.480(1)(d). According to KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the Sheriff and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution.

HARLAN COUNTY
NOTES TO FINANCIAL STATEMENT
May 31, 2006
(Continued)

Note 2. Deposits (Continued)

Custodial Credit Risk - Deposits

Custodial credit risk is the risk that in the event of a depository institution failure, the Sheriff's deposits may not be returned. The Sheriff does not have a deposit policy for custodial credit risk but rather follows the requirements of KRS 41.240(4). As of May 31, 2006, all deposits were covered by FDIC insurance or a properly executed collateral security agreement.

Note 3. Tax Collection Period

The real and personal property tax assessments were levied as of January 1, 2005. Property taxes were billed to finance governmental services for the year ended June 30, 2006. Liens are effective when the tax bills become delinquent. The collection period for these assessments was September 28, 2005 through May 31, 2006.

Note 4. Interest Income

The former Harlan County Sheriff earned \$7,278 as interest income on 2005 taxes. The former Sheriff distributed the appropriate amount to the school district as required by statute, and the remainder will be used to operate the Sheriff's office.

Note 5. Sheriff's Add-On Fees

The former Harlan County Sheriff collected \$43,085 of add-on fees allowed by KRS 134.430(3). This amount will be used to operate the Sheriff's office.

Note 6. Advertising Costs And Fees

The former Harlan County Sheriff collected \$1,566 of advertising costs allowed by KRS 424.330(1) and KRS 134.440(2). The former Sheriff distributed the advertising costs to the county as required by statute, and the advertising fees will be used to operate the Sheriff's office.

Note 7. Unrefundable Duplicate Payments And Unexplained Receipts Should Be Escrowed

The former Sheriff should deposit any unrefundable duplicate payments and unexplained receipts in an interest-bearing account. According to KRS 393.110, the Sheriff should properly report annually to the Treasury Department any unclaimed moneys. After three years, if the funds have not been claimed, the funds should be submitted to the Kentucky State Treasurer. For the 2005 taxes, the Sheriff had \$193 in unrefundable duplicate payments and unexplained receipts and for 2005 unmined coal taxes, the former Sheriff had \$343 in unrefundable duplicate payments and unexplained receipts. There was a balance of \$4,942 in the account as of July 24, 2007, for surplus money from prior years, which resulted in a total surplus of \$5,478. Therefore, the former Sheriff should send a written report to the Treasury Department.

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF THE FINANCIAL
STATEMENT PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS



CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

The Honorable Joseph A. Grieshop, Harlan County Judge/Executive
Honorable Steve Duff, Former Harlan County Sheriff
Honorable Marvin Lipford, Harlan County Sheriff
Members of the Harlan County Fiscal Court

**Report On Internal Control Over Financial Reporting And On
Compliance And Other Matters Based On An Audit Of The Financial
Statement Performed In Accordance With Government Auditing Standards**

We have audited the former Harlan County Sheriff's Settlement - 2005 Taxes as of May 31, 2006, and have issued our report thereon dated July 24, 2007. The former Sheriff prepared his financial statement in accordance with a basis of accounting other than generally accepted accounting principles. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the former Harlan County Sheriff's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statement and not to provide an opinion on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statement. The reportable condition is described in the accompanying comment and recommendation.

- The Former Sheriff's Office Lacked Adequate Segregation Of Duties

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statement being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we consider the reportable condition described above to be a material weakness.



Report On Internal Control Over Financial Reporting And
On Compliance And Other Matters Based On An Audit Of The Financial
Statement Performed In Accordance With Government Auditing Standards
(Continued)

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the former Harlan County Sheriff's Settlement - 2005 Taxes as of May 31, 2006 is free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

This report is intended solely for the information and use of management, the Harlan County Fiscal Court, and the Kentucky Governor's Office for Local Development and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Crit Luallen", with a long horizontal flourish extending to the right.

Crit Luallen
Auditor of Public Accounts

July 24, 2007

COMMENT AND RECOMMENDATION

HARLAN COUNTY
STEVE DUFF, FORMER SHERIFF
COMMENT AND RECOMMENDATION

As of May 31, 2006

INTERNAL CONTROL – REPORTABLE CONDITION AND MATERIAL WEAKNESS:

The Former Sheriff's Office Lacked Adequate Segregation of Duties

The former Sheriff's office lacked an adequate segregation of duties. There was a limited staff size, which prevented adequate division of responsibilities. However, having one person solely responsible for these duties compromises the internal control structure of the sheriff's office. Having only one individual who is responsible for all duties increases the risk that misstatements or errors may occur and not be detected in a timely manner. The former Sheriff should have implemented the following controls to help offset the lack of adequate segregation of duties:

- Cash recounted and deposited by the Sheriff
- Surprise cash counts by the Sheriff
- Agree daily tax collection totals to deposit slip
- Employees required to take mandatory vacations
- The Sheriff delivers tax distribution checks and monthly tax reports to taxing districts
- The Sheriff receives a signed receipt documenting delivery

Former Sheriff's Response: Again for last time these small sheriff's offices lack monies/manpower to adequately fulfill all the duties you require by your audit standards.

Auditor's Reply: The professional auditing standards, which are set by the national standards boards, would not require additional money or manpower. As discussed above the former Sheriff could have offset his lack of segregation of duties by personally monitoring the duties performed by his deputy.

